Remarks by
Chairman Debbie Matz
National Credit Union Administration
to
Missouri Credit Union Association
Annual Advocacy & Business Meeting

Jefferson City, Missouri
March 23, 2010

Thank you very much. I'm delighted to join you, and it's a special honor to be here on such a momentous occasion – Rosie's final legislative meeting.

No one embodies the spirit of the credit union movement better than Rosie. For more than 10 years, Rosie's dedicated service has helped sustain and strengthen Missouri's credit unions. During Rosie's decade at the helm of MCUA, Missouri's credit unions have enjoyed an impressive growth rate of 57 percent. One of Rosie's outstanding traits is that she is a visionary in creating ways to help member credit unions. Last year, in the aftermath of the worst economic downturn since the Great Depression, Rosie somehow found a way to offer a $500,000 dues rebate! And she managed to do this while maintaining MCUA's solid financial performance and reserves.

In addition to her service to Missouri's credit unions, Rosie established a strong reputation among her peers nationwide, bringing her member-service values to her work as Chairman of the American Association of Credit Union Leagues. It was a fitting tribute when AACUL presented Rosie with this year's Eugene H. Farley League Leadership Award—an extraordinary and well-deserved national honor.

Allow me to thank you, Rosie, for your outstanding record of service to Missouri, to the entire credit union community.

[Lead the applause.]

Thanks in large part to Rosie and the MCUA team, Missourians can look with pride at the strength of your state's credit union industry. Your spirit of enterprise and commitment to member service are certainly alive and well among Missouri's 144 credit unions.

Here in "the Show-Me state," your industry's performance has shown significant strength. You have an admirably high proportion of healthy credit unions – 101 have a CAMEL 1 or 2. This represents nearly 90 percent of Missouri credit union assets. Your overall modest rate of delinquencies and charge-offs are indications of sound lending standards and good management at most of Missouri's credit unions, large and small.

You've compiled this strong record even at a time when Missouri's economy – like the nation's – has been under greater stress than at any time since the 1930s. The national stimulus package has been helping to breathe some new life into the economy – but Missouri's unemployment rate, hovering (like the nation's) in the 10-percent range, remains unacceptably high. The new job-creation package, signed by President Obama last week, will inject additional investments that will help spur employment and raise incomes for Main Street Missourians.

If there's a silver lining in the midst of this economic crisis, it is this: In a day-and-age when every other part of America's financial-services sector has seen its reputation tarnished, credit unions are still shining.

Credit unions have lived up to their Main Street values, throughout this economic downturn. Unlike Wall Street, you don't have to look at the stock-market tables to know what your value is.

Yet, over the past several years, no part of America's financial sector has been immune from the pressures of the financial crisis – and of the prolonged recession that it triggered. The credit union industry now confronts an array of challenges that will test your resilience.

As the federal agency that ensures the safety and soundness of the credit union system, NCUA is committed to helping you through those challenges. It's certainly in America's best interest to have a strong, sustainable credit union industry – providing capital to hard-working families and good, solid businesses. When people get the credit they need to turn their dreams into reality, they can create what our country needs most, right now: good jobs for Main Street Americans.

Today, I'd like to discuss some of the challenges that are ahead for credit unions – and to explore how, by working together, we can try to turn today's challenges into tomorrow's opportunities.

I've been in my new role at NCUA for seven months now. When President Obama asked me to come back to the agency, where I had served as a Board member from 2002 to 2005, I didn't hesitate for a second.

But what a difference there is, between the economic conditions when I first served on the Board and the landscape we face today. The credit-market turbulence that started in 2007 seemed to come out of the blue – causing a financial crash in 2008, and the deep economic slump of 2009.

We seem to have gotten past the worst of the downturn by now, and many of the key economic indicators are beginning to turn upwards. Nonetheless, it's going to take awhile to clean up all the wreckage caused by this crisis.

The statistics remain worrisome. Nationwide, the number of credit unions downgraded to CAMEL 4 and 5 almost doubled during the economic downturn – and those credit unions hold more than 5 percent of all insured shares. Even larger is the growing group of credit unions rated CAMEL 3, which now account for nearly 14 percent of all insured shares. Many of the 7,600 federally insured credit unions – while still well capitalized – will be draining capital this year, due to negative earnings. At the same time, delinquencies and loan losses continue to increase. Undoubtedly, these will lead to an increase in failures.

So NCUA is stepping up to the plate. Our examiners are carefully monitoring the call reports of all federally insured credit unions, looking for red flags.

Although, as I indicated earlier, the overall health of the credit union system is sound, we're watching for a number of specific warning signs that have caused failures in recent years. These include increases in delinquencies in member business lending, indirect lending, and loan participations. We're particularly concerned about credit unions that are not doing their own due diligence. If you make member business loans, you must do your own underwriting even if you use a vendor or CUSO. If you make indirect loans, you must not delegate loan approval authority. And if you participate in loans, you still must do your own due diligence, even if the originator is another credit union.

We have asked our examiners to review call reports of every credit union. If they see that a credit union has suffered a significant increase in delinquencies in any of these areas, they will visit the credit union – even if an exam is not on the regular schedule.

We're also looking very closely at any institutions that are holding too many fixed-rate, long-term mortgages on their books. We've been warning, for months now, that higher interest rates are a question – not of "if" – but of "when." And you've seen, just in the past few weeks, that the Federal Reserve is indeed beginning to raise interest rates. So — for those of you here today who are credit union executives — we urge you to take action now make sure your portfolio is strong enough to withstand the interest-rate risks that will soon hit your balance sheet.

I know that some of you think NCUA is over-reacting. But the reality is: We're taking precautions to prevent dangerous situations from arising before it's too late. We're taking the disciplined steps that are needed to protect the credit union system as a whole.

With our careful oversight, our examiners don't intend to play a regulatory game of "gotcha." We must uphold rigorous standards – at credit unions large and small – because we aim to protect the 90 million members who depend on the safety and soundness of the credit union system.

If the recent financial meltdown taught us anything, it's that – particularly in financial services – weakness, whether real or perceived, can trigger ripple effects very quickly. That's why we don't ever want you to be in a place where any cracks start showing.

There will be positive long-term benefits from our continuing efforts to strengthen the system. During the recent years of stress, we've spent a great deal of time addressing credit unions' immediate problems. But, as we look ahead toward an economic recovery, we can again appreciate the industry's longer-term potential.

Because we've insisted on taking precautions early – before dangerous situations arise – all of us now have stronger reason for long-term optimism. We've taken many of the necessary steps to strengthen the system. The assessments to preserve the insurance fund and to stabilize the corporate credit union system – painful as they have been in the short term – will put the overall system in a stronger position for the long term.

(pause)

Even as we position the credit union system for a prosperous future, let me underscore one of the central challenges that we now confront, as we try to resolve the problems of the past.

As you know, NCUA has taken bold, decisive action to deal with the corporate credit union crisis. Yes – it was indeed a crisis. If we had not confronted the situation head-on – if we had allowed the corporate crisis to become a consumer crisis – the nation’s credit union system would have faced a grave systemic risk.

Let me take just a couple of minutes to explain – in straightforward terms – what occurred, and the steps we’re now taking to make sure that such a crisis can never happen again.

I’d like to start by assuring you that I fully recognize the legitimate anger that many of you feel about the corporate crisis. That anger has come through loud and clear in the comments we’ve received to the proposed new corporate rule, and in the town hall meetings we’ve held. In personal conversations with many of you, I’ve heard about the pain you have felt, amid the damage to the credit unions you’ve worked so hard to build. I know many of you blame NCUA – after all, two examiners were on site at US Central and WesCorp. I understand that. But there’s plenty of blame to go around. NCUA shares some of that blame. So do the managers and boards of those corporates who exercised such poor judgment.

Much of the blame falls outside the credit union industry. Mortgage brokers made questionable loans that led to waves of foreclosures. Rating agencies handed out AAA ratings for mortgage-backed securities that are now known as “toxic assets.” When this mortgage bubble burst, the fallout caused an extraordinary and unforeseen decline in the global economy.

But it’s not productive to look back to assess blame. It’s only productive to look back for the purpose of learning from our mistakes so we don’t repeat them. That’s what NCUA has been doing for the past year, as we developed the proposed corporate rule and asked for your comments.

I know you're all living with the consequences of the corporate failures. So I think it would be helpful to take a few minutes to explain how the corporate crisis unfolded. Some of the points are somewhat technical, but I'd like to help you gain a better understanding of exactly what took place, and to explain the thinking behind the key elements of our proposed rule.

The global credit crisis of 2007 and 2008 exposed the four giant corporate credit unions to extreme shock, because they held a vast amount of residential-mortgage-backed securities. When the market for those bonds suddenly plummeted, the corporates' losses pushed them toward insolvency.

If the corporates had abruptly stopped operating, that would have threatened to end the services they've long provided to natural-person credit unions. That's because three-quarters of natural-person credit unions have used the corporates as their primary agents for clearance and settlements – taking care of the complicated "financial plumbing" behind services like checking accounts, debit accounts and ATM transactions.

Worse: About 90 percent of natural-person credit unions had investments in the corporates. If the corporate system had collapsed, the natural-person-credit-union system would have suffered huge and insurmountable losses – shattering confidence in all of America's credit unions. Since they had such large investments in the corporates, they would have lost about $30 billion in net worth – about one-third of the net worth of all natural-person credit unions. This would have led to the collapse of at least 800 – perhaps as many as 1,200 – natural-person credit unions.

In addition, your federal Share Insurance Fund would have had to levy huge assessments on the remaining credit unions, in order to cover the remainder of the losses. It's uncertain whether those remaining credit unions could have withstood the strain. They would have been facing enormous costs in terms of capital and a catastrophic loss of public confidence.

We simply could not let that happen. As a result, NCUA had to put two of the largest corporates – US Central and WesCorp – into conservatorship. And we've also had to carefully monitor the operations of the other large corporates that are under severe pressure.

Then, to stabilize the entire credit union system, NCUA placed guarantees on shares at all corporates. This ensures that your credit unions' investments in Missouri Corporate and any other corporates are backed by the full faith and credit of the United States government.

Our aim has not been to "bail out" the corporates: We aimed to stop them from bleeding, as their assets were hemorrhaging value. NCUA did what we had to do, to save the system. We preserved public confidence. We stabilized the corporates.

Going forward, we must ensure that never again will the entire credit union system be threatened by one group of credit unions – or even one single credit union.

For the long term, NCUA is focused on providing a framework for safety and soundness that protects the system. We're determined to enact new safeguards to make sure that such a situation can never happen again.

The NCUA Board released the proposed new rule on corporates on November 19. By the time the public comment period closed on March 9, we had received over 800 comment letters, totaling over 2,500 pages. I assure you, we will read every one.

By contrast, the proposed rule runs 234 pages. Let me distill, for you, the proposed new rule into its four main themes. It involves changes in four critical areas that are flawed in the current rule.

First: On capital standards: The new rule will significantly strengthen capital requirements, aligning corporates with Basel One standards; subjecting corporates to a leverage capital requirement in an effort to reduce risk; and imposing Prompt Corrective Action standards on corporates that match those that apply to all other federally insured financial institutions.

Second: On asset-liability management: It proposes specific ALM requirements to ensure that the gap between the average life of assets and liabilities does not present excessive risk. It also prohibits a corporate from accepting funds from a single source that exceeds 10 percent of the corporate's assets. This will avoid excessive reliance on a single lender or depositor.

Third: On risk concentration: It will limit risk by forbidding corporates from excessive concentration in a single type of asset. Promoting a diverse portfolio of investments will help avoid the kind of risk concentration that was permitted under the flawed corporate rule that was approved in 2002. I voted against that rule for this very reason.

Fourth and finally: On governance standards: It will raise eligibility standards for corporates' board members, aiming to elevate the boards' level of experience, expertise and motivation.

Achieving our goals in these four areas will go a long way toward preventing another corporate crisis from ever occurring.

We've benefitted from the broad public input on these ideas, not only from your written insights during the public comment period, but also from your direct feedback in "town hall meetings" and a town hall webinar. Let me assure you: In light of all those comments, we will be making further improvements to the rule.

We're aiming to finalize the rule this summer. We're confident that the new safeguards, when refined and implemented, will protect the system from the threat of another meltdown.

But first, we plan to respond to what your comments told us is the highest priority: the need for NCUA to dispose of the toxic assets that caused the meltdown.

Isolating these so-called "legacy assets" – which are severely impaired securities – is a necessary first step in avoiding further damage, as we weigh various options for the best way to deal with them for the long term.

I understand why some of you do not want to recapitalize corporates as long as toxic assets remain on their books. And I understand why you are frustrated that

NCUA has not yet announced a plan to remove these legacy assets. So today, I'm going to share with you our plans to date.

First, let me say, this is very much a work in progress. It is an enormous undertaking.

There is no easy way to un-bundle over $50 billion worth of long-term assets, repackage them into marketable bonds, and move them from corporates' balance sheets without realizing the losses.

This effort is so huge – and so important – that we are dedicating 20 of our top staff to work on it. Over the past several months, our team has been brainstorming every idea they can imagine to safely resolve the corporate crisis at the lowest possible cost to credit unions. With nearly every possible solution, more questions and more legal and accounting issues are raised.

Yet today we feel we are on the verge of a breakthrough. Our team is close to proposing a plan that would remove the riskiest legacy assets from ongoing corporates, while carrying forward the most valuable pieces of the corporate system. The plan would empower natural-person credit unions to choose which corporates they will support. And it would ensure that those corporates begin with clean balance sheets.

If the plan proceeds as we envision, it could even allow credit unions to recover future earnings from legacy assets that out-perform current loss projections.

Our team is still working to answer a multitude of questions – questions about underwriting, funding, and much much more.

But they are cautiously optimistic that this careful process will generate the best possible answers. In fact, they hope to bring a comprehensive corporate resolution plan to the NCUA Board by the end of June.

Like you, I want to unveil NCUA's plan to resolve the corporate crisis as quickly as possible. But I do not want to rush this critically important process. We may only have one chance to get this right. So please bear with us until we are sure we have the best possible answers.

In the meantime, let me assure you again: We hear you loud and clear! Based on your comment letters, we will not move forward with a final corporate rule until after the plan for legacy assets is announced. And while the legacy assets plan will ensure that corporates begin with clean balance sheets, the final rule will ensure that corporates maintain those clean balance sheets.

(pause)

Looking ahead: There will be difficult choices – both for natural-person credit unions and for NCUA – about what to do for the future of corporates.

Let me underscore this priority: NCUA's overriding objective is to create a solid framework for safety and soundness. That's the surest way to protect your 90 million members.

Ultimately, the future of the corporate system will be determined by all of you – the leaders of natural person credit unions.

You will soon be facing the choice of either recapitalizing a corporate or finding other ways to obtain the same type of services that corporates have provided. We recognize that after experiencing losses on such a scale, it may be difficult for some credit union boards to make the decision to recapitalize a corporate.

All I can do is reassure you: After we dispose of the legacy assets and approve the final rule, corporates will be much better positioned to protect your hard-earned capital.

We recognize that the search for alternative providers would pose hard choices, especially for smaller credit unions.

As you're confronting these difficult choices, NCUA is ready to work with you as a constructive partner.

(pause)

After hearing about the severity of the recent crisis – and after the past few years' worth of gloom-and-doom headlines about the American economy – you're probably wondering: How on earth does she reconcile all those negatives with her belief that credit unions are facing positive prospects ahead?

The reason is simple. Along with most economists, I believe that we've already endured the worst of the economic downturn. There are still some rough times to come. But we’ve survived the worst. And we’ve taken strong measures to make sure that credit unions, and the system that frames them, will remain sound.

Now that the system is ready to bounce back, your industry can begin to chart a bold and confident course.

Building on your record of service and success, you’re positioned to broaden your appeal to millions of potential new members. The energy and spirit of innovation in the credit union community give me confidence that the industry has a bright future.

After the global crisis tarnished the reputation of every other part of the financial-services sector, Americans’ confidence in credit unions continues to grow. That’s a tangible measure of the faith that American families continue to place in credit unions. More and more consumers recognize that strong, transparent, well-run credit unions offer them access to some of the highest-quality, lowest-cost choices in the world of financial services.

We can all be proud of the pivotal role that credit unions play in meeting the needs of savers and borrowers in your local communities.

In a spirit of partnership – drawing on the faith that millions of Americans place in their credit unions – I’m looking forward to working closely with you in the years ahead to help you make the most of the opportunities that your industry enjoys, and to help you provide the benefits that America’s consumers deserve.

Thank you very much.